



Filing Receipt

Received - 2021-11-01 12:35:16 PM
Control Number - 52373
ItemNumber - 233

PROJECT NO. 52373

**REVIEW OF WHOLESALE ELECTRIC
MARKET DESIGN**

§
§

**PUBLIC UTILITY COMMISSION
OF TEXAS**

**COMMENTS OF
OCTOPUS ENERGY**

COMES NOW Evolve Retail Energy LLC d/b/a Octopus Energy (Octopus Energy), REP License #10262, and files these Comments in response to the Commission's Questions for Comment filed in this proceeding on October 26, 2021.

INTRODUCTION

Octopus Energy started as a Retail Electric Provider (REP) in ERCOT in 2019 as Evolve Energy which was renamed as Evolve Retail Energy. In 2020, Octopus Energy, based in the UK, purchased Evolve Retail Energy, and the Commission approved the company's name change just after Winter Storm Uri on February 22, 2021. Octopus Energy serves over three million customers globally and has been significantly expanding its operations in ERCOT. Octopus Energy is one of the few REPs that have made demand response a central tenant in the services we offer to our customers. Octopus Energy passes on financial benefits in the form of bill credits or lower prices to customers who respond to grid alerts. As Octopus Energy expands its presence in ERCOT, we increasingly will enable our customers to be partners with the Commission and ERCOT to ensure reliable operations in ERCOT rather than just being "load" that must be served as if it has no price elasticity.

On October 19, 2021, Octopus joined with many other stakeholders in the ERCOT market in a filing supporting the Commission's efforts to reform the ERCOT market to avoid future sustained load-shed of like that Texans endured this past February during Winter Storm Uri.¹ We support the Commission taking decisive action to address the specific problems that caused and contributed to the February disaster, such as the Commission's recent adoption of Phase 1 of its weatherization requirements,² considering

¹ ERCOT Stakeholders Reliability & Market Design Improvement Recommendations (Oct. 19, 2021).

² *Rulemaking to Establish Electric Weatherization Standards*, Project No. 51840 (Oct. 26, 2021).

changes to the Operating Reserve Demand Curve and high system-wide price cap, and improving the procurement and use of Emergency Response Service to increase grid reliability. We also support ERCOT's actions to improve reliability of the grid, such as expanding the opportunity for energy storage and load resources to provide reliability services. As was described in the joint filing on October 19, additional No Regrets actions the Commission can take include enabling the use of demand response, distributed generation, and distributed energy storage to provide reliability services to the grid. Octopus uses all of these tools to help customers reduce their energy spend on an individual basis and enabling the use of these on an aggregated basis to support grid reliability is a key step the Commission and ERCOT could take to increase reliable grid operations. In addition, supporting the efficient use of electricity so that Texans do not needlessly waste the state's resources would help reduce strain on the electric grid in both the winter and the summer.

COMMENTS

2. What modifications could be made to existing ancillary services to better reflect seasonal variability?

The highest residential demand generally occurs in the summer and winter months due to extreme temperatures and the increased air conditioning and heating that results. If ERCOT were to enable the use of aggregated residential demand response as part of its ancillary service procurement in these seasons, it would have additional tools to address seasonal variability on the grid. If ERCOT also were to ensure that aggregated distributed generation and energy storage also were able to participate in ERCOT's ancillary services, the grid would have even more flexibility to address grid reliability throughout the year. Key issues that ERCOT must address to take advantage of these aggregated resources is addressing cost-prohibitive telemetry and metering requirements, ensuring that the minimum size of aggregations is reasonable, and allowing aggregated resources to limit their potential dispatch to match their capabilities (e.g., do not require residential aggregations to reduce their load more than a reasonable amount of time, and allow the stacking of demand response tranches of demand response to meet longer duration needs).

3. **Should ERCOT develop a discrete fuel-specific reliability product for winter? If so, please describe the attributes of such a product, including procurement and verification processes.**
 - a. **How long would it take to develop such a product?**
 - b. **Could a similar fuel-based capability be captured by modifying existing ancillary services in the ERCOT market?**

Based on the failure of all generation technologies during Winter Storm Uri, a fuel-specific reliability product for winter could provide the façade of reliability with no actual substance behind it. For example, a natural gas reliability product that relies on “firm” contracts for natural gas to operate in extreme conditions would provide no greater reliability to the system than the natural gas plants that failed during Winter Storm Uri when their “firm” providers reportedly declared force majeure events to excuse their failure to provide fuel. Even nuclear and coal resources proved to not be “firm” during this winter event.

If ERCOT determines that a specific reliability product should be created for the winter, it should be fuel-neutral and require a certain level of on-site fuel or other energy supply, such as energy storage resources, that will be able to enable the resource to provide energy to the grid regardless of what fuel supply constraints or limitations occur in real time. However, reliance on traditional on-site fuel supplies like coal should not qualify to provide this service. Coal generators could not access their coal supplies during Winter Storm Uri due to frozen coal piles. In addition, ERCOT should ensure that the resources that offer to supply this service are weatherized to ensure reliable operation in harsh conditions. Not only should equipment not be susceptible to freezing in extremely cold windy weather conditions, but precautions should be taken to avoid any other situations due to winter weather conditions that Texas generators have experienced in the past, such as air intakes becoming blocked by frozen steam exhaust. Finally, all preparations should be subject to on-site inspection, verification, and extensive unannounced testing to ensure ERCOT receives the reliability it is procuring and representing to the public will protect them from future outages.

4. **Are there alternatives to a load serving entity (LSE) Obligation that could be used to impose a firming requirement on all generation resources in ERCOT?**

Octopus Energy opposes any firming requirement being imposed on existing generation in the ERCOT Region as well as resources that already have invested in the development process. Retroactively

imposing significantly new operating requirements (or contractual obligations) on existing resources can destroy the economics that supported the private capital invested to bring these resources to the ERCOT market, regardless of the type of generation at issue. Such action also would be a significant disincentive to future investment in the state as the risk that additional arbitrary, adverse changes could be made would dramatically increase the cost of capital. Financial markets depend on predictable rules. Retroactively changing requirements would likely significantly impact capital formation in the ERCOT markets.

In the event the Commission determines that a firming requirement should be imposed on all generation resources and mandates all resources operate at an established percentage of their nameplate capacity, such a requirement should be prospective only so that future developers and investors can take the additional cost into account to determine whether it would be economically reasonable to invest in the development of new generation resources in the ERCOT Region.

6. How can an LSE Obligation be designed to protect against the abuse of market power in the wholesale and retail markets?

ERCOT already has become an extremely consolidated market with a few market participants controlling the vast majority of generation resources as well as REPs. An obligation on load serving entities to buy capacity from generators when there is no obligation on the generators to sell their capacity naturally skews the market and gives generators undue leverage over load serving entities – especially REPs that compete against the generators’ affiliated REPs. Even if a generator does not have more than 20% of the installed nameplate capacity in ERCOT by today’s standards, the measure of market power could be dramatically greater when measured against the proposed regulatory weighting of one form of generation resource compared to another. Corporations with both generators and REPs within the same corporate family, especially when the generator has more capacity under its control than needed to serve the load of its affiliated REPs, will have a state-sanctioned competitive advantage over REPs that are not affiliated with generators. The notion of a competitive wholesale market in ERCOT consisting of willing buyers and willing sellers will be severely damaged, if not eliminated. Moreover, the lack of transparency of private

bilateral transactions will make it difficult for ERCOT or the IMM to ensure that market power is not being abused.

- a. Will an LSE Obligation negatively impact customer choice for consumers in the competitive retail electric market in ERCOT? Can protective measures be put in place to avoid a negative impact on customer choice? If so, please specify what measures.**

Yes, the proposed LSE Obligation will negatively impact customer choice for consumers in the ERCOT market. As discussed above, the proposed obligation will provide REPs that are affiliated with generators a significant advantage over REPs that are not so affiliated. The fact that a REP may be forced by the state to procure capacity from its competitor's affiliated generator provides that generator (and its affiliated REP) undue market power compared to the unaffiliated REP.

The proposed LSE Obligation is skewed to favor the status quo, including incumbent generators and affiliated REPs. The very generation resources that would be prioritized in this proposal are in large part the same assets that the incumbent generators own. This proposal is an attempt to use regulatory processes to force more cash into those assets. With the "favorable assets" cornered in the market by existing gen-tailers, the clearing price for these assets could be very expensive, effectively leading to a wealth transfer from small competitive REPs directly to large REPs and their affiliated generators. This will collapse long term competition.

The proposed LSE Obligation also can be expected to impose a significant credit squeeze on competitive REPs. New REPs in ERCOT generally must rely on third parties for access to credit necessary to participate in the ERCOT market. Credit often is sized on about one year of mark-to-market cash needs (plus ERCOT postings). This proposal could mean that the credit needs of small REPs would have to expand by up to three times their current requirements if the obligation to procure resources starts three years prior to when the resources will be required. Credit facilities are three to five year agreements, so for those REPs who entered into a facility in the past year or two, they easily could be limited in how much they can grow just because their credit facility may now be burdened by this new forward procurement obligation that is up to three times more than their originally expected needs. This would reduce growth of

competitive REPs by one-third of their historical potential and can be expected to collapse long term competition.

This credit squeeze could be further intensified to the extent that traditional sources of credit in the ERCOT market, such as large incumbent market participants, reduce the extent to which they provide credit facilities to small retailers. Following Winter Storm Uri, reduced sources of credit as well as tighter credit requirements, has been an issue. As a result, increasing credit requirements through the LSE Obligation in a market with fewer credit providers means this LSE Obligation proposal will negatively impact future competition.

Octopus Energy expects that the proposed LSE Obligation will lead to bad results for Texas consumers. If REPs are mandated to procure generation capacity up to three years before the capacity will be needed, REPs essentially will be forced to match their customer contracts to that same procurement cycle. In general, when a REP sells a one-year fixed price contract to a customer, a fiscally responsible REP will secure supply (or otherwise hedge) to match the long-term obligation they have committed to and plan to recover the costs for this hedging activity through higher commodity prices. The REP also often imposes an early termination fee in order to protect themselves for this additional expense in case the customer chooses to take service from an alternate REP before the end of the contracted term of service. The reverse also can be expected to be true – if a REP is required to start procuring supply for its customers three years in advance of the service to be provided, the REP will be incented to impose a long duration contract (three years) with a larger termination fee to protect themselves against the cost of the obligation the state has mandated. The longer duration contracts and termination fees that may be up to three times larger – possibly over \$1,000 per household – and will discourage customer shopping. Reduced customer shopping also can be expected to reduce the number of competitive REPs and the innovation they bring to the market.

8. Can the reliability needs of the system be effectively determined with an LSE Obligation? How should objective standards around the value of the reliability-providing assets be set on an on-going basis?

If the Commission's objective is to ensure reliability of the electric grid through the LSE Obligation, then the answer is no. Even the proponents of the LSE Obligation fully recognize that market design does not ensure reliability: "While many of the physical causes of those events may be beyond the reach of electricity market design (e.g., challenges with natural gas delivery)...".³ Nothing about the proposed LSE Obligation would have prevented the blackouts Texans suffered during Winter Storm Uri.

The authors of the proposed LSE Obligation suggest three challenges that the ERCOT system faces:⁴

1. Ensuring Sufficient Reliable Generation
2. Ensuring Resource Performance
3. Adapting to Higher Penetrations of Renewables

The Commission can quickly solve Challenges 1 and 3 by more timely approval of interconnection requests dispatchable generation resources submit to ERCOT (as well as all other interconnection requests). There currently are more than 34 GW of energy storage resources that are in the process of interconnecting in the ERCOT Region. While not all of these are expected to be built, the addition of a significant amount of energy storage, as well as all the other generation resources that are in development, can address these issues.

As far as resource performance (Challenge 2), the market signals exist in the electricity market to encourage the performance of all resources. In addition, the recently approved weatherization rules the Commission has adopted⁵ will ensure resources are better able to perform in adverse weather conditions. Unfortunately, the performance of all resources can be undermined by a lack of fuel, including uranium, coal, gas, water, wind, solar, etc., as well as mechanical difficulties, as seen during Winter Storm Uri. While the Commission has been working on rules that could improve reliability of upstream fuel supplies for gas-

³ Comments of Energy and Environmental Economics (Sept. 30, 2021) (hereinafter "LSE Reliability Obligation Proposal") at 6.

⁴ *Id.* at 7.

⁵ *Rulemaking to Establish Electric Weatherization Standards*, Project No. 51840 (Oct. 26, 2021).

fired generators, it generally been recognized that the primary responsibility to achieve weatherization for the natural gas industry lies with the Railroad Commission which has proposed rules that may not lead to much, if any, weatherization of that fuel supply despite its failure during Winter Storm Uri. The very generation resources the proposed LSE Obligation seeks to promote (nuclear, coal, and natural gas), all experienced significant operational difficulties during Winter Storm Uri.

9. How can the LSE Obligation be designed to ensure demand response resources can participate fully and at all points in time?

There are two types of demand response – economic and administrative. The proposed LSE Obligation will not enable the optimal use of economic demand response because it only provides credit to an LSE towards its procurement obligation for demand response that can be “curtailed or interrupted at the direction of the system operator.”⁶ Economic demand response occurs in response to market signals and, while some amount of it can be expected to be available, the extent to which it will actually be available at the exact time ERCOT calls for it will depend on the specific circumstances at the time. As a result, it is not clear that this form of demand response can be used to reduce the procurement obligations that this proposal would impose on REPs. Once a REP has been forced to procure energy that otherwise could be expected to be curtailed through economic demand response, the incentives of the REP and the customer to engage in this form of demand response will be muted since the additional cost to procure capacity already will have been incurred.

A dynamic grid will have different needs for demand response. A requirement for a demand response action to be available for two hours is a one-size fits all solution and will be insufficient.⁷ In contrast, allowing a REP to stack multiple customers for 15-minutes at a time will provide greater flexibility and also should also be sufficient. However, this later stacked approach may be more difficult to “prove” ahead of time, especially if it is not commercial and industrial demand response.

⁶ LSE Reliability Obligation Proposal at 28.

⁷ *See id.* at 39.

10. How will an LSE Obligation incent investment in existing and new dispatchable generation?

Octopus Energy does not expect that the LSE Obligation will incent investment in new dispatchable generation. It takes many years to develop fossil fuel assets. It takes decades to develop nuclear generation. While solar generation and solar collocated with energy storage can be built in a matter of months, the LSE Obligation and proposed discounting of the value of solar and energy storage assets will discourage those very investments.

11. How will an LSE Obligation help ERCOT ensure operational reliability in the real-time market (e.g., during cold weather events or periods of time with higher than expected electricity demand and/or lower than expected generation output of all types)?

Octopus Energy does not anticipate that an LSE Obligation will ensure operational reliability in the real time market during high demand situations. First, this is a capacity market in disguise. Just like other capacity markets, the LSE Obligation can be expected to dull energy price signals which also will dull the impact of demand response, which is one of the best tools we have to ensure future grid reliability.

13. What is the estimated market and consumer cost impact if an LSE obligation is implemented in ERCOT? Describe the methodology used to reach the dollar amount.

At this point, there is inadequate information available to calculate the true cost of the proposed LSE obligation on Texas consumers. However, qualitatively, it should be recognized that any uplift in generation payments will be paid by consumers since they ultimately pay for electricity consumed in Texas. As discussed above, the need for additional working capital will increase operating costs for REPs that will be passed on to consumers, and significantly higher early termination fees are a reflection of normal operating practices in the market.

15. If the Commission adopts an LSE Obligation, what assurances are necessary to ensure transparency and promote stability within retail and wholesale electric markets?

Octopus Energy expects that many small REPs that are not affiliated with generators will exit the ERCOT market if the Commission imposes an LSE Obligation. In light of the credit squeeze that this will impose as well as the danger of market power abuse, it is not clear that there are any “assurances” the Commission could offer that would make continued participation in the market economically viable.

Conclusion

As Octopus Energy and many other ERCOT Stakeholders indicated in their October 19 filing, there are many initiatives that the Commission has completed and has underway that can meaningfully increase reliability of the ERCOT electric grid. These are substantial “No Regrets” improvements. The proposed LSE Obligation is not one of those initiatives – there are real concerns about the adverse impact it could have on retail competition in the ERCOT market. This is not a proposal that the Commission should rush to embrace.

Octopus Energy appreciates the opportunity to provide these Comments and looks forward to working with the Commission and other interested parties on these issues.

Respectfully submitted,



Michael J. Jewell
Jewell & Associates, PLLC
State Bar No. 10665175
8404 Lakewood Ridge Cove
Austin, TX 78738
(512) 423-4065
(512) 236-5170 (FAX)
ATTORNEY FOR OCTOPUS ENERGY

PROJECT NO. 52373

**REVIEW OF WHOLESALE ELECTRIC
MARKET DESIGN**

§
§

**PUBLIC UTILITY COMMISSION
OF TEXAS**

COMMENTS OF OCTOPUS ENERGY

EXECUTIVE SUMMARY

- The Commission has made significant progress to improve reliability of the electric grid since Winter Storm Uri. Consistent with the Joint Filing made on October 19, 2021, that Octopus Energy joined, Octopus Energy continues to support Commission efforts to increase the use of demand response, distributed generation, and distributed energy storage to provide reliability services to the grid. Increased energy efficiency is a building block to support additional demand response in the market and also helps customers reduce the needless waste of the state's resources.
- ERCOT should include aggregated demand response, distributed generation, and distributed energy storage as part of its ancillary services procurement to better reflect seasonal variability of demand.
- If ERCOT develops a reliability product for winter, the requirements should be fuel-neutral, require a certain level of on-site fuel or other energy supply to secure performance in adverse weather conditions, and require that the resources providing the service are weatherized and have taken precautions against other situations that Texas generators have experienced resulting from severe weather conditions.
- Octopus Energy opposes a firming requirement being imposed on existing generation as well as resources that already have invested in the development process. Retroactive requirements would significantly adversely affect capital formation in the ERCOT market.
- The proposed LSE Obligation would increase the market power of incumbent thermal generators and their affiliated REPs. The forward procurement obligation would impose a significant credit squeeze on competitive REPs. The notion of a competitive wholesale market in ERCOT consisting of willing buyers and willing sellers would be severely damaged if not eliminated.
- The proposed LSE Obligation would damage retail competition in the ERCOT Region and increase costs for customers due to the need for higher early termination penalties and higher operating costs for REPs. REPs likely would need to impose longer terms to contracts for service which will discourage customer shopping.
- The LSE Obligation would discourage economic demand response in the market. The proposed accreditation for administrative demand response is likely to discourage the use of residential demand response.
- The Commission could address the challenges identified by the proponents of the LSE Obligation through implementation of the weatherization rules the Commission already has adopted as well as improvements to the ERCOT interconnection process and ensuring clear market signals in the wholesale energy market.